IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 45.

THE UNITED STATES, *Petitioner*,

v.

THE KANSAS FLOUR MILLS CORPORATION, *Respondent*.

On Writ of Certiorari to the Court of Claims.

BRIEF FOR THE RESPONDENT.

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OPINION BELOW.

The opinion of the Court below (R. 9) is reported in 92 Ct. Cls. 390.

JURISDICTION.

The judgment of the Court of Claims was entered January 6, 1941 (R. 10). The petition for a writ of certiorari was filed March 31, 1941 (R. 10) and was granted May 12, 1941 (R. 11). The jurisdiction of this Court rests on Section 3(b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

QUESTIONS PRESENTED.

During the period from May 1935 to January 6, 1936, the respondent sold and delivered flour to various Government agencies under contracts containing a clause which recited that the prices "include any Federal tax heretofore imposed by the Congress," and provided that if any taxes are thereafter "imposed or changed by the Congress," then the contract price will "be increased or decreased accordingly." The Government paid the contract price. The respondent had enjoined the collection of processing taxes on the wheat used to manufacture the flour and was relieved of the payment of said taxes when they were held invalid by the decision of this Court on January 6, 1936.

The Government withheld funds admitted to be owing to the respondent for flour sold and delivered to Government agencies subsequent to January 6, 1936 and applied said funds to an alleged indebtedness of respondent resulting from failure to pay the processing taxes on wheat processed for the period from May 1935 to January 6, 1936. Under these circumstances the following questions are presented:

1. (a) Does the language of the contract construed in accordance with recognized principles require an adjustment of the sales price of the flour sold and delivered during the period from May 1935 to January 6, 1936, because of the invalidity of the processing taxes, even though that condition was not specified in the contract?

(b) Was the enactment of Titles III, IV and VII of the Revenue Act of 1936 a "change by the Congress" contemplated by the contract?

2. Assuming that the language of the contract does not require a price adjustment with respect to the flour sold and delivered to Government agencies during the period from May 1935 to January 6, 1936, does the Government have the right to exact a price adjustment by withholding funds belonging to respondent on equitable grounds where it is not shown:

(a) That there was any mistake by the parties, but only a recognized doubt, as to the validity and collectibility of the processing taxes, or

(b) That any particular part of the burden of the processing taxes was shifted to the Government in the contract price of the flour sold and delivered from May, 1935 to January 6, 1936?

3. May the Government here assert for the first time equitable grounds in support of a claimed set-off where it was not pleaded or considered in the Court of Claims or mentioned in the petition for certiorari?

STATEMENT.

Respondent is a corporation organized and existing under the laws of the State of Delaware with its principal office in Kansas City, Missouri and at all times mentioned herein was engaged in the business of manufacturing flour and related products from wheat for sale to various buyers including the United States. (R. 6) The respondent sold to the United States under contracts dated May 12, June 27, July 31 and December 4, 1936, wheat flour and wheat bran for a total consideration of $23,288.11. (R. 6-7) The flour and bran were delivered and accepted by the United States and vouchers in the amount of $23,288.11 were forwarded to the General Accounting Office for payment. (R. 6-7) The payment of these vouchers was withheld by the Comptroller General and the amount credited by him against an alleged indebtedness of a larger amount on account of alleged overpayments made by the petitioner to the respondent under certain other contracts. (R. 6-7)

The other contracts were entered into and completed during the period from May, 1935 to January 6, 1936, under which the respondent sold to the United States approximately 3,383,000 pounds of flour. The flour was sold to the United States at a composite price, and the tax was not separately invoiced as appears in an excerpt from one of

the contracts between the respondent and the United States typical of the price provision contained in all of the contracts of sale and in all the invoices issued to the United States by the respondent as follows: (R. 7)

Item	Pounds (about)	Unit price (per pound)	Total contract price
Lb. Flour, wheat, in sacks, Type A	78,400	0.0323	$2,532.32

Each of the contracts contained the following provision: (R. 7)

> "Prices set forth herein include any Federal tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract, and are paid to the Government by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly, and any amount due the contractor as a result of such change will be charged to the Government and entered on vouchers (or invoices) as separate items."

The respondent delivered the flour under the contracts, the same was accepted by the United States and payment made therefor in accordance with the bid price. (R. 7) Along with other wheat processors the respondent had during the period from May, 1935 to January 6, 1936 applied for and obtained from the United States District Court an injunction prohibiting the Collector of Internal Revenue from the collection of any processing taxes from it during this period. (R. 8)

The Secretary of Agriculture prior to May, 1935 in accordance with authority vested in him by the provisions of the Agricultural Adjustment Act of May 12, 1933 (48 Stat. 31), as amended, had, by Wheat Regulations approved by

the President, established the rate of tax on first domestic processing of wheat at 30 cents per bushel of wheat processed. The conversion factor as applied to floor stocks of flour was fixed at .704 cents per pound. (R. 8)

The petitioner has identified certain contracts entered into between it and the respondent during the period from May, 1935 to January 6, 1936 and by multiplying the total number of pounds of flour provided for by the contracts by the conversion factor applicable to floor stocks, .704 cents per pound, has arrived at an amount of the alleged indebtedness of the respondent to the United States amounting to $28,419.20. (R. 8) The amount for which judgment has been rendered, $23,288.11, which is admitted to be owing to the respondent, had been credited by the Comptroller General against the alleged indebtedness of the respondent to the United States in the amount of $28,419.20. (R. 8-9) On April 20, 1938 a petition was filed in the Court of Claims by the respondent to recover the $23,288.11 owing to it by the United States on account of flour delivered and accepted under contracts subsequent to January 6, 1936. The Government entered a general traverse. (R. 5) The Court of Claims entered judgment in favor of the respondent in the amount of $23,288.11 on January 6, 1941. (R. 10)

SUMMARY OF ARGUMENT.

The Government's case is founded on two erroneous assumptions. In the first place, the Government assumes that both parties to the contract supposed that "respondent was liable for and would pay the processing tax to the United States." (Br. p. 24) On the contrary, during the period from May, 1935 to January 6, 1936, when the contracts were signed and payments made, the parties clearly had in mind the possibility that the processing tax was invalid and that respondent might be relieved of payment, since respondent actually had an injunction against collection of the processing tax during that period. One Circuit Court of Appeals held the tax invalid and this Court granted a tem-

porary injunction against collection during the same period. Moreover, the Comptroller General had considered the possibility of the invalidity of the processing tax in connection with contracts containing similar tax clauses, which he ruled made no provision for price adjustment in the event of a decision of invalidity.

The Government also assumes that the full burden of the processing tax was shifted in the selling prices specified in the contracts. The determination of the extent to which the tax burden was shifted is a very difficult and complex question of economic fact, involving a comparison of actual prices with the prices that would have prevailed in the absence of the tax. No evidence was offered on the subject and it cannot be assumed *a priori* that the selling prices were higher, by the full amount of the tax, than they would have been if there had been no tax.

The provisions in the contracts for price adjustment are clear and specific and do not require any reduction in the prices under the circumstances of this case. The tax clause provides for a price reduction only in the event that taxes of the kind described should be "changed by the Congress." Respondent was relieved from payment of the processing tax by reason of this Court's decision holding the tax invalid, and not as a result of any change by Congress. *United States* v. *Butler*, 297 U. S. 1. The Revenue Act of 1936, enacted more than five months after this Court held that collection of processing taxes should be enjoined, was not such a change by Congress within the meaning of the clause.

There is no unexpressed purpose of the tax clause that would justify a reduction of the contract prices here. It cannot be said that the purpose of the clause was to protect the parties against *all* contingencies affecting margins or prices, in the face of an enumeration of specific contingencies that would call for price adjustment. Compare *United States* v. *Glenn L. Martin Co.*, 308 U. S. 62; *United States* v. *Cowden Mfg. Co.*, 312 U. S. 34. Nor is there any basis for the Government's argument that another purpose of

the clause was "to give the Government the certainty that increased or decreased tax collections would be precisely offset by corresponding price changes." (Govt. Br. p. 6) If there had been ary such purpose it could easily have been expressed.

There is no merit to the Government's argument that a set-off should be allowed on equitable grounds without regard to the tax clause. The relief claimed is based on an alleged mutual mistake of the parties as to the validity of the processing tax. However there was no mistake, but only a recognized doubt as to the validity of the tax, collection of which respondent had enjoined. Equitable relief is not granted in such a case.

Moreover, restitution would in any event be limited to the amount of tax burden shifted, which has not been shown. Respondent would not be unjustly enriched by avoiding that part of the tax burden which it had failed to shift as an economic fact.

The imposition of the unjust enrichment tax would constitute a "change in circumstances" which would preclude the claimed restitution if otherwise allowable. Under Section 501(b) of the Revenue Act of 1936, Respondent would *not* be entitled to an exclusion from income subject to the 80 per cent tax on the basis of a repayment to the Government at this time, if such repayment is based on grounds of equity or quasi-contract,—without regard to the tax clause in the contracts.

With the exception of one case, which is pending here on petition for certiorari, there are no authorities supporting the Government's position. Numerous decisions deny recovery to buyers in similar cases where goods are sold at a composite price. The *Wayne County Produce Co.* case which petitioner cites, points out the distinction between cases like the present and the situation there involved where goods were sold at a named purchase price and the buyer agreed in addition to pay a sales tax which was mistakenly believed to be applicable but which was later refunded.

Petitioner did not assert any equitable ground in the Court of Claims nor in the petition for certiorari. This Court's consideration of the case should therefore be limited to Petitioner's rights on the contracts as written.

ARGUMENT.

I.

PETITIONER'S CASE IS FOUNDED UPON THE ERRONEOUS ASSUMPTIONS THAT (1) THE PARTIES FAILED TO CONTEMPLATE THE INVALIDITY OF THE PROCESSING TAX AND (2) THAT THE FULL BURDEN OF THE TAX WAS SHIFTED IN THE SELLING PRICE.

There are two fallacies running through the Government's argument and forming an essential part of the Government's case. In the interest of clear thinking these fallacies should be exposed before we undertake to answer the Government's argument in detail. The Government's brief assumes:

(1) that the parties to the contracts did not contemplate the possible invalidity of the processing tax, and

(2) that the full burden of the processing tax was shifted by respondent in the selling prices specified in the contracts.

It is submitted that both of these assumptions are without foundation in fact, so that the Government's entire argument based upon these premises is unsound.

(1) There Was No Mutual Mistake, but Only a Recognized Doubt as to the Validity of the Processing Tax.

In the first place, the contracts were entered into "during the period from May, 1935 to January 6, 1936" and during that period Respondent had an injunction "prohibiting the collection from it of any processing taxes". (R. 7, 8.) The question as to the validity of the processing tax had been in litigation for a long time prior to that period

and at least one District Court had passed upon the question as early as October 19, 1934. *Franklin Process Co.* v. *Hoosac Mills*, 8 F. Supp 552 (D. Mass.). A Circuit Court of Appeals had actually held the processing tax invalid on June 13, 1935. *Butler et al.* v. *United States*, 78 F. (2d) 1 (C. C. A. 1). A temporary injunction was granted in this Court on November 25, 1935. *Rickert Rice Mills, Inc.* v. *Fontenot*, 296 U. S. 569, 297 U. S. 110. Under these circumstances, there is no basis for the Government's argument that the parties did not contemplate the possible invalidity of the tax "during the period from May, 1935 to January 6, 1936" when the various contracts were signed.

Moreover, in the summer and fall of 1935 the Comptroller General had given consideration to the possibility of a judicial determination of invalidity, in passing on and approving contracts similar to those involved here, where the tax clauses were modified by bidders. In a decision rendered September 12, 1935, particular reference was made to the fact that "the legality of such (processing) taxes is now in the Courts", but the Comptroller General said this with reference to the possibility of judicial determination of invalidity:

> "Such a determination by the Courts would not constitute a change in the tax 'by the Congress', as contemplated in the formal invitation for bids, but a judicial determination that a tax theretofore imposed is not legal." A-64860, 15 Dec. Compt. Genl. 201.

Another decision to the same effect was rendered on November 4, 1935, A-66872, 15 Dec. Compt. Gen. 367. The clause there considered was expressly stated to be the clause in Government Standard Form No. 33, Short Form Contract, which is substantially identical with the clause used in the contracts in this case.[1]

Not only was the possible invalidity of the processing tax contemplated by the parties, but the administrative officers

[1] See Code of Federal Regulations, Title 41, Sec. 12.33.

of the Government definitely considered this possibility with particular reference to the tax clause in the Government Standard Form No. 33, which was held not to require any price adjustment on the basis of a judicial determination of invalidity. The basic assumption made throughout the Government's brief is therefore utterly unfounded.

(2) It Cannot Be Assumed a Priori that the Full Tax Burden Was Shifted.

In the second place, there is no basis in the facts of this case for the assumption made by the Government that the full burden of the processing tax was shifted by Respondent in the selling price specified in the contracts. It may be admitted that the existence of the processing tax had some probable effect on the market price for flour fixed in open competition. Some part of the tax burden might have been shifted by processors, and by respondent in particular, in the sense that their selling prices were higher because of the tax than they would have been if the tax had not been imposed.[2] However, there is no basis for assuming, without proof, that the whole or any particular part of the tax burden was thus shifted.[3] It will be shown later that the Government's claim for equitable relief, if otherwise

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[2] See the introduction to Seligman, "*The Shifting & Incidence of Taxation*" (5th ed. 1926); Carver, "*Principles of National Economy*" (1921), p. 630; Shultz, "*American Public Finance & Taxation*" (1932), p. 277; Buehler, "*Public Finance*", 2nd ed. 1940, pp. 344 et seq.; Hunter, "*Outlines of Public Finance*" (1936), pp. 154 et seq.; Brown, "*The Economics of Taxation*" (1924), pp. 9-13, 56 et seq.; Lutz, "*Public Finance*" (3 ed. 1936), pp. 381, et seq. See also Ferger, "*Windfall Tax and Processing Tax Refund Provisions* of the 1936 Revenue Act"; XXVII The American Economic Review, 45, 52; "*An Analysis of the Effects of the Processing Taxes Levied Under the Agricultural Adjustment Act*", prepared in the Bureau of Agricultural Economics (Govt. Print. Of. 1937) p. 1.

[3] One District Court found as a fact that the flour market was "demoralized" after May 1, 1935, as a result of attacks on the constitutionality of the Agricultural Adjustment Act, and that the processing tax applicable to flour sold after that date was "wholly absorbed" by the processor. *Johnson* v. *Scott County Milling Co.*, 21 F. Supp. 847, 849 (E. D. Mo.).

sound, must be limited to such part of the purchase price as represents the extent to which the economic burden of the processing tax was shifted to it.[4]

In the case of *Indian Motorcycle Co.* v. *United States*, 283 U. S. 570, 581, Mr. Justice Stone, dissenting, pointed out that no assumption can be made *a priori* that any particular tax at any particular time is passed on. Although this view was expressed in a dissenting opinion, the decision of the majority has since been discredited. Cf. *James* v. *Dravo Contracting Co.*, 302 U. S. 134, 170-171. However, even the majority in the *Indian Motorcycle Co.* case would hardly question Mr. Justice Stone's ideas in the case of a processing or manufacturing tax, as distinguished from the sales tax there involved. Cf. *Wheeler Lumber, Bridge & Supply Co.* v. *United States*, 281 U. S. 572; *Liggett & Myers Tobacco Co.* v. *United States*, 299 U. S. 383.

In any event, it is submitted that Mr. Justice Stone was absolutely correct when he made the following statement with reference to the assumption that the burden of a sales tax is inevitably passed on to the buyer:

> "With this assumption economists would not, I believe, generally agree. Many hold that whether the burden of any tax paid by the seller is actually passed on to the buyer depends upon considerations so various and complex as to preclude the assumption *a priori* that any particular tax at any particular time is passed on. In some conditions of the market, the burden remains with the seller, or even may be shifted back from the seller to the producer by the reduction of the producer's price rather than forward to the consumer by an increase of the seller's price."

It is true that the contracts in the present case recite that the contract prices "include any Federal tax heretofore imposed by the Congress". It is submitted, however, that such

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[4] The Government argues (Br. p. 24) that "Had the parties known that respondent was not liable for and would not pay the tax, the contract price would have been reduced accordingly." The assumption is that the price would have been lower by the full amount of the tax, an assumption without foundation.

an expression is no real evidence that the whole or any part of the economic burden of the tax was being shifted in the named prices. Goods are frequently sold at a price "including tax" in the sense that no further charge is to be made against the buyer on account of the tax. Such a provision may be particularly important in situations where taxes sometimes are, or have been, billed separately as an addition to a stated selling price. That was true in the case of goods produced from commodities subject to the processing tax during the early part of the tax period. Section 18 of the Agricultural Adjustment Act, 48 Stat. 31, 41, provided that where articles produced from a taxable commodity were delivered after the effective date of the processing tax under contracts of sale entered into before the date, the seller might add the amount of the tax to the invoice as a separate item to be collected from the buyer. Cf. *United States* v. *Cowden Mfg. Co.*, 312 U. S. 34, 35-36. In the case of contracts entered into later, a stipulation that the processing tax was included in the price gave the buyer assurance that there would be no additional charge on account of the tax. It is submitted that the recital in the contracts here was intended simply to furnish such a clarification.

It would be fantastic to suppose that the parties intended by the contract recital to express the opinion that the economic burden of the tax was being shifted in full in the contract prices. The parties would hardly have undertaken to express an opinion in the contract as to the extent to which the existence of the processing tax affected the market price for flour arrived at in open competition. The question as to the extent to which the processing tax was shifted in such selling prices must be recognized as a very complicated and difficult question of economic fact, involving a comparison between the actual prices, and the prices that would have prevailed in the absence of the tax.[5]

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[5] The Congressional Committees which reported Title VII of the Revenue Act of 1936, limiting refunds of processing taxes to the extent to which the claimants bore the burden of such taxes, said: "The question as to whether processing taxes were passed on • • •

The Government relies (Br. p. 27) on the recent decision of *United States* v. *American Packing & Provision Co.*, 122 F. (2d) 445 (C. C. A. 10th), pending in this Court on petition for certiorari, No. 735. In the Circuit Court of Appeals equitable relief was granted to the Government in a situation similar to that involved here. The Court in that case considered that the contract recital that prices "include any Federal tax" justified an inference that the tax burden had been shifted in the contract prices. However, the court did not indicate that it had any clear concept of tax shifting, and it is submitted that the decision is unsound. Contracts for the sale of hog products were involved there, and Government economists have published their finding that no appreciable part of the processing tax on hogs was reflected in the market price for hog products. See "*An Analysis of the Effects of the Processing Taxes Levied Under the Agricultural Adjustment Act*", prepared by the Bureau of Agricultural Economics and published by the Bureau of Internal Revenue (Govt. Print. Of. 1937). On page 9 of that report it is said:

> "Since the aggregate retail value of hog products consumed apparently was not changed by the tax, and the volume of hog products consumed was not materially affected, it follows that the retail prices of hog products were little, if any, higher with the tax than they would have been without the tax. * * * In other

involves extremely complicated economic and accounting considerations." *Senate Report No. 2156*, 74th Cong. 2nd Sess. p. 33; *House Report No. 2818*, 74th Cong. 2nd Sess., p. 2.

The Government contended in this Court in the *Anniston* case that the extent of tax absorption could be determined by "fair and reasonable approximations", but recognized that "the accounting and economic problems in some cases will be complex and difficult". *Anniston Mfg. Co.* v. *Davis*, October Term, 1936, No. 667 (Govt. Br. pp. 162-163).

The Bureau of Agricultural Economics has recognized that the determination of the incidence of processing taxes "involves some of the most complex considerations in the field of economics". *Analysis of the Effects of the Processing Taxes Levied under the Agricultural Adjustment Act* (Govt. Print. Of. 1937), p. 4. See also Ferger, *op. cit. supra*, Note 2, at pages 52-53.

words, if there had been no processing tax, the retail price of hog products would have been no different from what it actually was in both years when the tax was in effect."

Even if the recital that the prices include tax should be held to constitute *some* evidence of a complete shifting of the economic burden of the tax, which we deny, the Court of Claims has made no finding of the ultimate fact. The question as to the extent of shift is material to the ground which the Government asserts in this Court for the first time, based upon broad equitable considerations apart from the contract language. Since that ground was not asserted in the Court of Claims, it was not material for the parties to offer evidence on the extent to which the burden was shifted. It will be pointed out more at length later in this brief that the so-called equitable ground which the Government asserts cannot be sustained without a showing as to the extent to which the burden of the tax was shifted in the contract prices. It is submitted that there is certainly no basis for assuming in this case that the full amount of the burden of the tax was shifted in the contract price.

II.

THERE WAS NO CHANGE MADE BY THE CONGRESS OR OTHERWISE IN THE PROCESSING TAXES WITHIN THE LANGUAGE OR PURPOSE OF THE TAX CLAUSE.

Under the clear and express provisions of the tax clauses in the contracts, a reduction of the stated price is required only where the processing tax, or other imposition there described, is "changed by the Congress". (R. 7.) It is submitted that there was no such change in the processing tax within the meaning of the tax clause. Neither the invalidity of the processing tax, nor the judicial determination of invalidity, nor the alleged congressional recognition of invalidity, justifies any price reduction under the terms of the contracts.

(1) The Tax Clause Does Not Warrant a Price Reduction Based on Invalidity or Judicial Determination of Invalidity of Processing Taxes.

This Court held the Agricultural Adjustment Act unconstitutional and the processing tax invalid in *United States* v. *Butler, supra*, on January 6, 1936; and in *Rickert Rice Mills, Inc.* v. *Fontenot, supra*, decided on January 13, 1936, it was held that collection should be enjoined and the amounts impounded should be returned to the processors. Under these two decisions the processing taxes were never a legal liability and never were legally collectible. Judicial determination of invalidity was certainly not a change by Congress within the meaning of the tax clause.

The parties *could* have, but *did not* provide for a price adjustment on the basis of the invalidity, or the judicial determination of the invalidity, of the processing tax. If the parties had intended to provide for a price adjustment upon the basis of such a contingency, there would have been no difficulty in choosing apt words to express such an intent. For example, some sellers of articles produced from taxable commodities expressly stipulated in their contracts for price adjustments under certain circumstances in the event that this Court should determine that the processing taxes were invalid. See, for example, the contract involved in *Casey Jones Inc.* v. *Texas Textile Mills, Inc.*, 87 F. (2d) 454, 455, note 1 (C. C. A. 5th).

The possibility of a decision of invalidity was certainly in the minds of the parties, as we have demonstrated under proposition I, *supra*, where reference was made to the fact that during the period when these contracts were being entered into respondent had actually obtained an injunction against the collection of the processing taxes, and the Comptroller General had given consideration to the possibility with particular reference to contracts of the kind involved here. Moreover, we pointed out that one Circuit Court of Appeals had actually held the processing tax invalid, and that this court granted a temporary injunction against the

collection of processing taxes during the period in which these contracts were being signed, and yet, none of these contracts contained any provision that a decision of this Court holding the processing taxes invalid would be one of the conditions requiring price adjustment. There is, therefore, no possible basis for construing the language of the contracts as requiring a price reduction on the ground of invalidity or judicial determination of invalidity.

Even the court which held for the Government on equitable grounds in a similar situation, recognized that the tax clause itself did not justify a price reduction under the circumstances. See *United States* v. *American Packing & Provision Co., supra.*[6] A similar construction was given to the identical tax clause in *United States* v. *Hagan & Cushing Co.*, 115 F. (2d) 849 (C. C. A. 9th), and in *Ismert-Hincke Milling Co.* v. *United States*, 90 Ct. Cls. 27. The Government's brief here (p. 29) refers to a number of cases, involving similar, but not identical, clauses in contracts between private parties, in all of which cases the clauses contemplating price reductions to offset tax decreases are construed as not warranting recovery by the vendee after this Court's decision in the *Butler* case.[7] It is true that some of those cases involve other obstacles to the buyer's recovery,

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[6] That Court said: "There is nothing in the contract which has reference to the unconstitutionality of the tax or the annulment of the tax. The so-called 'up and down' or the 'increase and decrease' clauses have no relevancy to the unconstitutionality of the tax. It may be conceded that if the right of the Government to recover is dependent upon the contracts between the parties, it must fail." 122 F. (2d) at 449.

[7] *Moundridge Milling Co.* v. *Cream of Wheat Corp.*, 105 F. (2d) 366 (C. C. A. 10); *Consolidated Flour Mills* v. *Ph. Orth Co.*, 114 F. (2d) 898 (C. C. A. 7); *City Baking Co.* v. *Cascade Milling & Elevator Co.*, 24 F. Supp. 950 (D. Mont.); *G. S. Johnson Co.* v. *N. Sauer Milling Co.*, 148 Kan. 861; *Sparks Milling Co.* v. *Powell*, 283 Ky. 669; *Crete Mills* v. *Smith Baking Co.*, 136 Neb. 448; *Johnson* v. *Igleheart Bros.*, 95 F. (2d) 4 (C. C. A. 7), certiorari denied, 304 U. S. 585; *Noll Co.* v. *Sparks Milling Co.*, 304 Ill. App. 624; and *Southern Biscuit Co.* v. *Lloyd*, 174 Va. 299. See also *United States* v. *American Packing and Provision Co.*, 122 F. (2d) 445, 449 (C. C. A-10).

but they all recognize that where tax clauses make no reference to a decision of invalidity, they cannot be construed as requiring price reduction on the basis of such a contingency.

(2) The Revenue Act of 1936 Did Not Constitute a Change by Congress of the Processing Taxes, Within the Meaning of the Tax Clause.

The Government's brief refers to the *Butler* decision on January 6, 1936, holding the processing tax unconstitutional and the *Rickert Rice Mills* decision on January 13, 1936, upholding injunctions against the collection of processing taxes, and then urges that "Congress thereafter (in the Revenue Act of 1936 approved June 22, 1936) both recognized and participated in the elimination of the tax liability". We might concede for the sake of argument that Congress at that time recognized the invalidity of the processing tax but it is ridiculous to say that Congress "participated in the elimination of the tax liability". Although an unconstitutional statute may have some factual consequences (Cf. *Chicot County Drainage District* v. *Baxter State Bank*, 308 U. S. 371), it cannot be said in the face of the *Butler* decision that the Agricultural Adjustment Act created any tax liability, *Norton* v. *Shelby County*, 118 U. S. 425; *Hopkins* v. *Clemson College*, 221 U. S. 636. After the decisions of this Court in the *Butler* and the *Rickert* cases, Congress could do nothing toward eliminating the tax liability.[8] There is no basis for suggesting that respondent's failure to pay the processing taxes with respect to the flour sold to the Government was due in any way to changes made by Congress. There were some factual consequences of the unconstitutional Agricultural Adjustment Act which furnish the basis for the imposition by Congress of the new

[8] In the petition for certiorari here the Solicitor General made no claim that Congress "participated" in the termination of liability, but contended merely that the Revenue Act of 1936 constituted a congressional recognition of the termination of the processing tax program.

liability for unjust enrichment tax under Title III of the Revenue Act of 1936. However, factually, realistically and practically, Congress contributed nothing to the termination of the processing taxes or to the relief of respondent from paying them. There was therefore no change by Congress within the meaning of these contracts.

As a matter of fact, Title III of the Revenue Act of 1936 makes no mention of processing taxes as such or the Agricultural Adjustment Act. It is applicable generally to cases where any "Federal excise tax was imposed . . . but not paid." Internal Revenue Code, Sections 700-706. It is not limited to cases of invalid or unconstitutional excises—the reason for nonpayment is not material. Title III, therefore, is not even a recognition by Congress of the termination of processing taxes or their invalidity.

Titles IV and VII of the Revenue Act of 1936, to which the Government's brief also refers, cannot constitute any change by Congress in the processing taxes "applicable directly upon the production" of the flour delivered to the Government, within the meaning of the tax clause. As the Government's brief points out, Title IV relates to floor stocks, export and charitable refunds and therefore could have no possible bearing on the processing taxes applicable to the flour here involved. Indeed, the floor stocks provision of 602(a) mentioned by the Government (Br. p. 13), is not available to processors but only to persons who were not liable for the tax.

Title VII relates only to processing taxes that were actually paid to the Government. Even as to such collections, there is no admission in Title VII that the taxes were invalid. Restrictions are there imposed on refunds that might be allowable without regard to the ground of invalidity. That Title would apply to overpayments of processing taxes, even if the Agricultural Adjustment Act were constitutional. Title VII is similar in this connection to Section 3443(d) of the Internal Revenue Code, relating to refunds of other excise taxes.

It is submitted, therefore, that there is nothing in the Revenue Act of 1936 which would constitute a change by Congress within the meaning of the contracts.

(3) There is no Broad Unexpressed Purpose of the Tax Clause that Would Justify a Reduction of the Contract Price.

Clauses similar to those involved in the present case have been construed literally and narrowly by this Court in two cases decided in favor of the Government. *United States* v. *Glenn L. Martin Co.*, 308 U. S. 62; *United States* v. *Cowden Mfg. Co.*, 312 U. S. 34. In both of those cases the Government urged that the clauses should be construed literally so as to deny price increases to the contractor on the basis of new tax burdens that affected the contractor's margin of profit adversely. In urging in the present case that a reduction in the contract price is justified under similar clauses on account of the invalidity of the processing tax, which was not at all unanticipated, the Government argues (Br. p. 6) that "the obvious purpose of the tax clause was to insure to the contractor a stable margin of profit". The clauses were certainly not intended by the parties, to insure a fixed margin of profit, or any profit at all. The clauses in these contracts did not purport to protect either party against *all* contingencies affecting margins or prices, any more than the identical clauses in the *Cowden* and *Martin* cases. The seller was not expected to be protected from sudden and unanticipated increases in wages or other costs, and the buyer was not to be protected against a sudden drop in the price of the raw commodity which would have cheapened the supplies covered by the contract. If there had been any intention to insure to the contractor a stable margin of profit that intention could easily have been expressed in the contract. As the Government argued in the *Glenn L. Martin Co. case*, "the parties could have agreed to do business on a cost-plus basis, but they did not see fit to do so. Cf.

Cramp and Sons Ship Co. v. *U. S.*, 72 Ct. Cl. 146". Government brief pp. 10-11 in *United States* v. *The Glenn L. Martin Co.*, October Term 1939, No. 30. See also Government brief pp. 9-10 in *United States* v. *Cowden Mfg. Co.*, October Term 1940, No. 188.

The truth of the matter is that the clauses in all of these cases were designed to protect the seller and buyer against certain contingencies which were specifically enumerated. Thus, the clause provided for a price increase if a new tax, of the kind described, should be "imposed" by Congress. It also provided for an increase or decrease in price upon the basis of a change in the rate of processing taxes pursuant to the Act of Congress. The Agricultural Adjustment Act contemplated and expressly provided for changes in the rate of processing tax at intervals, depending upon the relationship between the farm price of a taxed commodity and its fair exchange value, as defined in the Act. See Section 9, Agricultural Adjustment Act of 1933 (48 Stat. 31, 33-34).[9] These are contingencies covered by the tax clause. The language of the clause, however, is specific and there is absolutely no basis for reading into the contracts an unexpressed intention to cover some other kind of contingency affecting prices.

The same thing is true of the other unexpressed purpose which the Government argues (Br. p. 6) was behind the tax clause, namely, "to give the Government the certainty that increased or decreased tax collections would be precisely offset by corresponding price changes".[10] If that had been

[9] Actually there was no change in the rate of processing tax on wheat, but changes were made under the Act with reference to other commodities. *Cf. T. D. 4518*, XIV-1 C. B. 450; *T. D. 4495*, XIII-2 C. B. 515.

[10] In the *Cowden Manufacturing Company* case, the Government did not argue that an identical tax clause had any such purpose. There the Government actuallly collected the processing tax, which was imposed after the contract was signed and which was separately billed to the contractor. There was no suggestion in the Government's argument in that case, or in this Court's opinion, that the increase in tax collections was to be offset by a corresponding price change.

a purpose of the contracts it could easily have been expressed. There would have been no difficulty in providing that the selling price should be reduced in a certain amount if the contractor should avoid the payment of the processing taxes. As we have pointed out, the possible invalidity of the processing tax was clearly in the minds of the parties, and the Comptroller General had actually ruled that such a contingency was not provided against in the tax clause of the Government Standard Form of Contract. Where the contracts were thus noticeably silent on the invalidity of the processing tax or the avoidance of payment by the contractor, the courts cannot read into the contracts an unexpressed intention to adjust prices on the basis of such contingencies.

III.

THE GOVERNMENT IS NOT ENTITLED TO RECOVER ON EQUITABLE GROUNDS WITHOUT REGARD TO THE LANGUAGE OF THE TAX CLAUSE.

In the Government's brief on the merits here, the contention is raised for the first time that, without regard to the tax clause, the United States can recover on grounds of equity or quasi-contract. Although we show later that the Court should give no consideration to such a ground, since it was not raised in the court below nor in the petition for certiorari, we will establish that there is absolutely no merit in the Government's contention.

(1) Equitable Relief is Not Granted on Account of a Recognized Doubt.

The Government's so-called equitable ground is based upon an alleged "mutual mistake of the parties". The Government contends (Br. p. 24) that "it was supposed by both parties that Respondent was liable for and would pay the processing tax to the United States". That contention is the core of the Government's case and it is utterly without foundation in fact. Not only is there no evidence of such a

mistake, but we have shown that the parties very definitely had in mind the possibility that the processing tax might be held invalid and might never have to be paid. Under these circumstances, there is no basis for equitable relief on the ground of mistake. Williston, "*Contracts*" (Rev. ed.) Sec. 1543; Pomeroy, "*Equity Jurisprudence*" (4th ed.) Sec. 855; American Law Institute Restatement, "*Contracts*", Sec. 502, comment f; "*Restitution*", Sec. 10(1), comment a, and Sec. 11(1).

The established principle, and the common sense view, is thus stated in comment f, under Section 502 of the Restatement on Contracts:

> "Where the parties know that there is doubt in regard to a certain matter and contract on that assumption, the contract is not rendered voidable because one is disappointed in the hope that the facts accord with his wishes. The risk of the existence of the doubtful fact is then assumed as one of the elements of the bargain."

It may be that the Government was confident that it would win the *Butler* case, and it no doubt was disappointed at the outcome. There must have been some doubts on the part of the Government as to the decision which the Supreme Court would render on the question as to the validity of the processing tax. In comment a, under Section 10(1) of the Restatement on Restitution, it is said:

> "Even slight doubt as to the existence of the subject matter of a contract will prevent restitution, since it may be assumed that the provisions of the contract were inserted with such doubt in mind, and that if the transferor had intended the contract to be conditional, he would have so specified."

The fact that respondent actually had an injunction against the collection of the processing tax during the period when the contracts were signed is conclusive evidence that the parties recognized the possibility that respondent might not pay the tax to the United States. The Govern-

ment's case for recovery "without regard to the tax clause" must therefore fall in the absence of a mistake that would give rise to equitable relief.

(2) Restitution in Any Event Would Be Limited to the Amount of Tax Burden Shifted, Which Has Not Been Shown.

However, even if there had been an actionable mistake, the Government has failed to show the extent to which respondent might have been benefited or the Government hurt by it. The recovery of a payment made on the ground of mistake is based essentially on the theory that one party "has been unjustly enriched at the expense of another". American Law Institute, Restatement, "*Restitution*," Sec. 1. The extent of respondent's enrichment resulting from its avoidance of the payment of the tax could not exceed the portion of the tax burden shifted to the Government in the stated contract price. To the extent that respondent failed to shift some part of the tax burden, respondent received no benefit or enrichment from its failure to pay that part of the tax to the Government. We have already shown that it cannot be assumed *a priori*, or under the facts of this case, that the full economic burden of the processing tax was shifted to the Government in the contract prices.[11] Even if there had been a mistake,—if the parties had assumed that there was no question as to the validity of the tax and the inevitability of its payment—the Government should be denied recovery in the absence of a showing as to the extent to which it was hurt or the respondent was benefited through a shifting of the burden in the contract prices.

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[11] Even to the extent that some part of the tax burden was shifted in the contract prices, it cannot be said that the benefit to respondent from non-payment of the tax was an *unjust* enrichment since, as we have shown, the possibility of avoidance of the tax was in the minds of the parties when they contracted. It is only reasonable to conclude that the tax had a lesser effect on the market prices of flour than it would have had if payment of the tax had been considered inevitable.

It may be pointed out that the amount of set-off claimed by the Government "was arrived at by applying the conversion factor of .704 cents per pound to the total amount of flour" delivered under the contracts. (Govt. Br. p. 3.) The processing tax, of course, was not imposed on the flour, but upon the processing of wheat, and at the rate of 30 cents per bushel of wheat. The factor of .704 cents was determined by the Secretary of Agriculture and the Treasury Department as being the rate applicable to a pound of flour, for purposes of the floor stock and compensating taxes, and for computing refunds under certain exemption provisions of the Agricultural Adjustment Act. *T. D. 4391*, XII-2 C. B. 480; *T. D. 4579*, XIV-2 C. B. 483, 487. The rate of .704 cents per pound of flour is computed by assuming an average yield of one barrel of flour (196 pounds) from 4.6 bushels of wheat (60 pounds per bushel, or a total of 276 pounds). The difference in weight between the flour and the wheat, namely, 80 pounds (276—196), is accounted for by the by-products, bran or middlings. However, the full amount of tax on the 4.6 bushels of wheat, namely, $1.38 (4.6 bu.×$.30) was attributed by the Secretary of Agriculture to the flour in order to arrive at the rate of .704 cents per pound of flour ($1.38 : 196 pounds); and none of the tax was apportioned to the bran or middlings, as the Treasury decisions cited above clearly show.

It appears therefore that the set-off claimed by the Government is based upon the assumption that the full amount of tax on wheat was shifted in the sale of flour. Even if it could be assumed that respondent, and millers generally, shifted the full burden of the tax, it could not be reasonably assumed that the full amount of the tax burden was shifted in the sale of flour and no part of it in the sale of bran or middlings.

The objection to the measure of recovery claimed by the Government is, however, much more fundamental and serious than that it fails to reflect the amount of tax on that part of the wheat that went into the flour delivered under the contracts. It is true that all of the taxable wheat did

not go into the flour, but some went into bran and middlings. Moreover, the Government has failed to show by proper evidence the quantity of wheat required by respondent to produce the quantity of flour delivered. But the fundamental and fatal objection to the amount of set-off claimed is that the Government has failed to show the extent to which the economic burden of the tax was shifted in the contract prices. What effect did the processing tax have on the market price of flour, the price fixed in open competition, at the times when the contracts were signed? To what extent were the selling prices higher than they would have been if there had been no tax? These questions would have to be answered, at least by reasonable estimates or approximations, on the basis of proper evidence, before the court could ascertain the extent to which respondent had shifted the tax burden, or the extent to which the Government had been hurt and respondent benefited. The Government offered absolutely no evidence on this subject and the Court of Claims made no finding of the ultimate fact as to the extent of shift. It is submitted therefore that the Government has not established a measure of recovery based on "unjust enrichment." The Government's case should fail for this reason even if the contracts or payments had been made under such mistake as would give rise to equitable relief.

(3) The Imposition of the Unjust Enrichment Tax Would Constitute a "Change in Circumstances" Which Would Preclude the Claimed Restitution if Otherwise Allowable.

Another infirmity in the Government's case for equitable relief may be found in the application to respondent of the unjust enrichment tax provisions of Title III of the Revenue Act of 1936. Section 501(a) of that Act imposes on respondent a tax at the rate of 80 per cent on "that portion of the net income from the sale" of the flour "which is attributable to shifting to others to any extent the burden of" the unpaid processing tax. [I.R.C.,

Sec. 700(a)]. The Government's brief (pp. 18-19) refers to these provisions, but urges that under Section 501(b) [I.R.C., Sec. 700(b)], respondent "would not be subject to the unjust enrichment tax on these transactions," "if it should be required to reduce its sales price by the amount of its unpaid processing taxes." This contention might be sound if the price reduction were made pursuant to the sales contracts themselves, and the Government made the contention only in the course of its argument that the tax clause in the contracts requires the adjustment. The contention would be unsound with reference to a repayment ordered on equitable grounds "without regard to the tax clause."

As the Government brief (p. 18) points out, Section 501(b) excludes from taxable income the net income from sales with respect to which the taxpayer made a "tax adjustment" with his vendee, and Section 501(j)(4) [I.R.C. Sec. 700(j)(4)] defines "tax adjustment" as a repayment "made on or before June 1, 1936, or thereafter in the *bona fide* settlement of a written agreement entered into on or before March 3, 1936." It is clear therefore that respondent would not be entitled to an exclusion, under Section 501(b), on account of a price reduction made after June 1, 1936, unless such reduction in price were made pursuant to a written agreement. If respondent is required to make repayment to the Government on equitable grounds, "without regard to the tax clause," the repayment will not justify an exclusion from income subject to the 80 per cent tax.

Even if the Government were otherwise entitled to restitution, the imposition by Congress of the unjust enrichment tax would constitute such a change in circumstances as would preclude recovery on equitable grounds. "*Restatement on Restitution*," American Law Institute, Secs. 69, 142. In Title III of the Revenue Act of 1936, Congress enacted a comprehensive plan for dealing with any possible unjust enrichment resulting from the invalidity of the processing tax. That title is applicable to sales of tax avoided goods, whether the sales were made to individual buyers or to the

Government. The gross inequity of the Government's claim here is emphasized by its dual role as buyer and as collector of the 80 per cent tax under Title III.

IV.

WITH THE EXCEPTION OF ONE DECISION, THE AUTHORITIES DO NOT SUPPORT PETITIONER'S CONTENTION.

With the exception of *United States* v. *American Packing & Provision Co., supra,* none of the cases cited by petitioner supports its position. The Government cites a number of cases on the subject of equitable relief based on mistake of law, with particular reference to suits by the Government. The cases have no bearing on the controversy, since we concede that money paid out by public officials may be recovered when payments are based on mistake of law as well as of fact. The point is that there was no mistaken of law or fact here. Not only has the Government failed to establish that there was any mistake, but it appears affirmatively that the parties recognized the possibility that the processing tax would be held invalid. There was no mistake, but only a recognized doubt as to respondent's liability for the tax, and as we have demonstrated there is no basis for equitable relief in such a case.

The case of *Wayne County Produce Co.* v. *Duffy-Mott Co.*, 244 N. Y. 351, cited by petitioner, involved a sale of cider at an agreed price of "14½ cents per gallon, subject to a stated discount, plus the manufacturer's war tax of 10 per cent which was to be paid in full without discount." The seller, "after collecting the amount of the tax from the plaintiff" (buyer), paid it to the Federal Government. It was later held by the courts in other cases that the tax was not applicable to cider, and the seller in the *Wayne County* case obtained a refund from the Government. The Court of Appeals held that the buyer could recover the amount of refund from the seller. Chief Judge Cardozo, writing the opinion of the court, based the relief on a mutual mistake of the parties and said:

> "The distinction is unimportant, at least for present purposes, between mistakes of fact and those of law. The quality of the mistake did not prevent the defendant from recovering the money from the Government. It cannot absolve from the duty of disposing of the money thus recovered as good conscience shall dictate."

There was no question in that case as to the existence of the mistake. It did not appear that there was any doubt as to the seller's liability for the tax when the contracts were signed and payment made. The court points out:

> "The Treasury Department and manufacturers generally had misconstrued an Act of Congress whereby a tax of 10% was levied upon sales of unfermented grape-juice and 'other soft drinks'."

The Chief Judge expressly distinguished the case before him, where the buyer agreed "to pay a stated price, and to put the seller in funds for the payment of the tax besides," from cases like the present, where the goods are sold at a composite price. He said:

> "This is not a case where the item of the tax is absorbed in a total or composite price to be paid at all events. In such a case the buyer is without remedy, though the annulment of the tax may increase the profit to the seller. *Moore* v. *Des Arts*, 1 N. Y. 359. This is a case where the promise of the buyer is to pay a stated price, and to put the seller in funds for the payment of a tax besides. In such a case the failure of the tax reduces to an equivalent extent the obligation of the promise. The form of the transaction was not thoughtless or accidental. It was deliberate and purposed. The end to be served is conceded in the brief of counsel. If a sum equal to 10% of the quoted price per gallon had been added to the price as something to be paid at all events, a tax would have been due upon the sum so added as well as upon the residue. The form was adopted whereby the manufacturer was in a position to account to the Government at a quoted rate per gallon, and to pay the tax with the excess. The defendant had the benefit of the transaction as thus molded in its dealings with the Government."

The case of *Moore* v. *DesArts*, which Chief Judge Cardozo cites with approval and distinguishes, involved a sale by an importer of goods on which the importer had paid a definite sum to the Collector for duties. The goods were sold by the importer at the "long price," so that under the usage and custom in the trade the buyer would be entitled to the drawback in the event that he should export the goods. Thereafter, the Secretary of the Treasury decided that the goods were free from duty, and the amount of duties collected was refunded to the seller. The buyer sought to recover the amount of refund from the seller. The court pointed out that the Government officers had decided both ways on the question whether the goods were subject to duty and said that "it may fairly be presumed that these merchants knew that was a debatable question; they knew that the decision made by the Collector might be overruled by the Secretary of the Treasury and the duties be refunded to the importer." On these facts the court denied recovery.

The court recognized that the agreed purchase price was subject to adjustment in some circumstances, namely, in the event of a drawback on export of the goods, but it was pointed out that there was no such drawback and that the agreement of the parties did not provide for a price reduction upon the basis of any other contingency.

A similar situation is involved in the present case. Here there was a debatable question whether the processing taxes were valid and the parties knew that there was a chance that this Court would relieve the contractor from the payment of the tax. The contract in the present case provided for an adjustment in price upon certain contingencies specifically set forth, and by like reasoning a reduction in price should be denied upon the basis of the invalidity of the tax which was not covered by the tax clause. The situation both in the present case and in *Moore* v. *DesArts* is therefore clearly distinguishable from the *Wayne County Produce case*, where the parties had misconstrued the tax act and there was no intimation that they had any doubt as to the applicability of the tax to the goods in question.

V.

PETITIONER'S CLAIM FOR EQUITABLE RELIEF, APART FROM THE CONTRACT, WAS NOT ASSERTED IN THE COURT OF CLAIMS NOR IN THE PETITION FOR CERTIORARI AND SHOULD RECEIVE NO CONSIDERATION HERE.

The Government argues here that it is entitled to recover on the ground of mutual mistake, "without regard to the tax clause" (Br. pp. 24-27), and "even if the tax clause were wholly ignored." (Br. p. 7.) This claim for equitable relief, or quasi-contractual recovery, based on an alleged mutual mistake, is raised by the Government in its brief on the merits here. It was not mentioned in the petition for certiorari[12] and was neither asserted nor considered in the Court of Claims. The only question raised or argued in the Court of Claims was whether the Government was entitled to a price adjustment under the terms of the tax clause in the written contracts. The Government's brief in the Court of Claims states the "question presented" thus:

> "*Whether under the eight contracts* entered into by the plaintiff and defendant during the period that the Agricultural Adjustment Act was in force, plaintiff has been overpaid by defendant in the amounts of the processing taxes on the supplies sold thereunder and included in the contract prices, by reason of the fact plaintiff did not pay such processing taxes." (Italics supplied.)

If the Government had relied on the equitable ground in the Court below, it would have been required to plead its defense affirmatively[13] and the burden of proof would have

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[12] The petition for certiorari herein was filed before the Circuit Court of Appeals for the Tenth Circuit decided the one case that supports petitioner's present theory of equitable relief. See *United States* v. *American Packing & Provision Co.*, *supra*. The Court in that case, however, was careful to point out that the Government had pleaded an "equitable set-off," which was not the case here. 122 F. (2) at 449.

[13] Court of Claims Rule 21.

been on it. *Jones* v. *United States*, 39 Fed. 410, 412. The Government would have to establish by evidence, (1) the existence of the alleged mutual mistake, and (2) the extent to which it was damaged thereby. This last element would have involved a showing of the probable price at which the parties would have contracted, if at the time it had been known with certainty that the processing tax was invalid and would not have to be paid. Of course, no evidence on the subject was offered and the Court of Claims made no finding of the facts essential to a recovery on the ground of mistake. If the Government had raised the point and offered some evidence in support of it, respondent would have had an opportunity to meet the Government's case with opposing evidence. As things stand, the only record fact bearing on the new defense is the finding by the Court of Claims that Respondent had an injunction against collection of processing taxes when the contracts were signed, a fact which completely negatives the existence of the asserted mistake.

Under the circumstances outlined above, it is submitted that this Court should apply the general principle that appellate courts should "confine themselves to the issue raised below". See *Hormel* v. *Helvering*, 312 U. S. 552, 556-558; *Helvering* v. *Wood*, 309 U. S. 344, 349; *Helvering* v. *Tex-Penn Oil Co.*, 300 U. S. 481, 498; *Helvering* v. *Minnesota Tea Company*, 296 U. S. 378, 380. See also "Raising New Questions on Appeal", 40 Harv. L. Rev. 907.

It is true that this Court will not apply the general principle "where the obvious result would be a plain miscarriage of justice" (*Hormel* v. *Helvering*, 312 U. S. at 558), but no such situation is involved here. Had the claim of mutual mistake, or unjust enrichment, developed during trial, there might have been fair opportunity for the respondent to present evidence in refutation or reduction of the counterclaim. The trial court might then have had some evidence upon which to make findings respecting it. But, when there is neither pleading, nor proof by the Government, and there is otherwise no suggestion to respondent

of any such defense, it would be notably severe to allow such a set-off first asserted in this Court. So to bind this respondent after trial in a suit at law, by an unsuggested equitable remedy founded upon mutual mistake and requiring affirmative proof, would in fact, settle upon the respondent the burden of anticipating and meeting in the trial any and every defense which might conceivably defeat its right of recovery. It is respectfully submitted that the allowance of the Government's contention here is not justifiable within the exception made in *Hormel* v. *Helvering*, *supra*.

Apart from the general rule against raising new points on appeal under circumstances requiring a remand for further proceedings, this Court has refused to consider grounds not presented in the petition for certiorari. *Gunning* v. *Cooley*, 281 U. S. 90; *General Talking Pictures Corporation* v. *Western Electric Co.*, 304 U. S. 175; *Dickinson Industrial Site, Inc.* v. *Cowan*, 309 U. S. 382. Since the Government failed to mention the equitable grounds in its petition for certiorari and the point was not raised or considered below, it is submitted that the refusal of this Court to consider it now will work no injustice, but will rather tend to promote the orderly course of litigation.

CONCLUSION.

It is, therefore, respectfully submitted that the decision of the Court below is correct and should be affirmed.

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November, 1941.

APPENDIX.

Budget and Accounting Act, 1921, 42 Stat. 20:

SEC. 305. Section 236 of the Revised Statutes is amended to read as follows:

"SEC. 236. All claims and demands whatever by the Government of the United States or against it, and all accounts whatever in which the Government of the United States is concerned, either as debtor or creditor, shall be settled and adjusted in the General Accounting Office." [U. S. C., Title 31, Sec. 71.]

Agricultural Adjustment Act, 48 Stat. 31, as amended:

SEC. 9 (a) To obtain revenue for extraordinary expenses incurred by reason of the national economic emergency, there shall be levied processing taxes as hereinafter provided. When the Secretary of Agriculture determines that any one or more payments authorized to be made under section 8 are to be made with respect to any basic agricultural commodity, he shall proclaim such determination, and a processing tax shall be in effect with respect to such commodity from the beginning of the marketing year therefor next following the date of such proclamation; * * *. The processing tax shall be levied, assessed, and collected upon the first domestic processing of the commodity, whether of domestic production or imported, and shall be paid by the processor. The rate of tax shall conform to the requirements of subsection (b). Such rate shall be determined by the Secretary of Agriculture as of the date the tax first takes effect, and the rate so determined shall, at such intervals as the Secretary finds necessary to effectuate the declared policy, be adjusted by him to conform to such requirements. The processing tax shall terminate at the end of the marketing year current at the time the Secretary proclaims that all payments authorized under section 8 which are in effect are to be discontinued with respect to such commodity. The marketing year for each commodity shall be ascertained and prescribed by regulations of the Secretary of Agriculture; * * *.

(b) (1) The processing tax shall be at such rate as equals the difference between the current average farm

price for the commodity and the fair exchange value of the commodity, plus such percentage of such difference, not to exceed 20 per centum, as the Secretary of Agriculture may determine will result in the collection, in any marketing year with respect to which such rate of tax may be in effect pursuant to the provisions of this title, of an amount of tax equal to (A) the amount of credits or refunds which he estimates will be allowed or made during such period pursuant to section 615(c) of this title with respect to the commodity and (B) the amount of tax which he estimates would have been collected during such period upon all processings of such commodity which are exempt from tax by reason of the fact that such processings are done by or for a State, or a political subdivision or an institution thereof, had such processings been subject to tax. If, prior to the time the tax takes effect, or at any time thereafter, the Secretary has reason to believe that the tax at such rate, or at the then existing rate, on the processing of the commodity generally or for any designated use or uses, or on the processing of the commodity in the production of any designated product or products thereof for any designated use or uses, will cause or is causing such reduction in the quantity of the commodity or products thereof domestically consumed as to result in the accumulation or surplus stocks of the commodity or products thereof or in the depression of the farm price of the commodity, then the Secretary shall cause an appropriate investigation to be made, and afford due notice and opportunity for hearing to interested parties. If thereupon the Secretary determines and proclaims that any such result will occur or is occurring, then the processing tax on the processing of the commodity generally or for any designated use or uses, or on the processing of the commodity in the production of any designated product or products thereof for any designated use or uses, shall be at such lower rate or rates as he determines and proclaims will prevent such accumulation of surplus stocks and depression of the farm price of the commodity, and the tax shall remain during its effective period at such lower rate until the Secretary, after due notice and opportunity for hearing to interested parties, determines and proclaims that an increase in the rate of such tax

pression of the farm price of the commodity. Thereafter the processing tax shall be at the highest rate which the Secretary determines will not cause such accumulation of surplus stocks or depression of the farm price of the commodity, but it shall not be higher than the rate provided in the first sentence of this paragraph.

* * * * * * * * *

[U. S. C. Supp. V, Title 7, Sec. 609.]

Sec. 18 (a) If (1) any processor, jobber, or wholesaler has, prior to the date a tax with respect to any commodity is first imposed under this chapter, made a bona fide contract of sale for delivery on or after such date, of any article processed wholly or in chief value from such commodity, and if (2) such contract does not permit the addition to the amount to be paid thereunder of the whole of such tax, then (unless the contract prohibits such addition) the vendee shall pay so much of the tax as is not permitted to be added to the contract price.

(b) Taxes payable by the vendee shall be paid to the vendor at the time the sale is consummated and shall be collected and paid to the United States by the vendor in the same manner as other taxes under this chapter. In case of failure or refusal by the vendee to pay such taxes to the vendor, the vendor shall report the facts to the Commissioner of Internal Revenue who shall cause collections of such taxes to be made from the vendee.

MISCELLANEOUS

SEC. 10. * * *.

* * * * * * * * *

(c) The Secretary of Agriculture is authorized, with the approval of the President, to make such regulations with the force and effect of law as may be necessary to carry out the powers vested in him by this title. Any violation of any regulation shall be subject to such penalty, not in excess of $100, as may be provided therein.

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[U. S. C. Supp. V, Title 7, Sec. 610.]

COMMODITIES

SEC. 11. As used in this title, the term "basic agricultural commodity" means wheat, rye, flax, barley, cotton, field corn, grain sorghums, hogs, cattle, rice, potatoes, tobacco, peanuts, sugar beets and sugarcane, and milk and its products, and any regional or market classification, type, or grade thereof; * * *.

[U. S. C. Supp. V, Title 7, Sec. 611.]

Revenue Act of 1936, 49 Stat. 1648:

SEC. 501. TAX ON NET INCOME FROM CERTAIN SOURCES.

(a) The following taxes shall be levied, collected, and paid for each taxable year (in addition to any other tax on net income), upon the net income of every person which arises from the sources specified below:

(1) A tax equal to 80 per centum of that portion of the net income from the sale of articles with respect to which a Federal excise tax was imposed on such person but not paid which is attributable to shifting to others to any extent the burden of such Federal excise tax and which does not exceed such person's net income for the entire taxable year from the sale of articles with respect to which such Federal excise tax was imposed.

(2) A tax equal to 80 per centum of the net income from reimbursement received by such person from his vendors of amounts representing Federal excise-tax burdens included in prices paid by such person to such vendors, to the extent that such net income does not exceed the amount of such Federal excise-tax burden which such person in turn shifted to his vendees.

(3) A tax equal to 80 per centum of the net income from refunds or credits to such person from the United States of Federal excise taxes erroneously or illegally collected with respect to any articles, to the extent that such net income does not exceed the amount of the burden of such Federal excise taxes with respect to such articles which such person shifted to others.

(b) The net income (specified in subsection (a) (1)) from the sale of articles with respect to which the Federal excise tax was not paid, and the net income speci-

fied in subsection (a) (2) or (3), shall not include the net income from the sale of any article, from reimbursement with respect to any article, or from refund or credit of Federal excise tax with respect to any article (1) if such article (or the articles processed therefrom) were not sold by the taxpayer on or before the date of the termination of the Federal excise tax; (2) if the taxpayer made a tax adjustment with respect to such article (or the articles processed therefrom) with his vendee; or (3) if under the terms of any statute the taxpayer would have been entitled to a refund from the United States of the Federal excise tax with respect to the article otherwise than as an erroneous or illegal collection (assuming, in case the tax was not paid, that it had been paid).

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(j) As used in this section—

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(2) The term "date of the termination of the Federal excise tax" means, in the case of a Federal excise tax held invalid by a decision of the Supreme Court, the date of such decision.

• • • • • • • • • •

(4) The term "tax adjustment" means a repayment or credit by the taxpayer to his vendee of an amount equal to the Federal excise tax with respect to an article (less reasonable expense to the vendor in connection with the nonpayment or recovery by him of the amount of such tax and in connection with the making of such repayment or credit) if such repayment or credit is made on or before June 1, 1936, or thereafter in the *bona fide settlement of a written agreement* entered into on or before March 3, 1936.

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SEC. 601. REFUNDS UNDER AGRICULTURAL ADUSTMENT ACT ON EXPORTS, DELIVERIES FOR CHARITABLE DISTRIBUTION OR USE, ETC.

(a) The provisions of sections 10 (d), 15 (a), 15 (c), 16 (e) (1), 16 (e) (3), and 17 (a) of the Agricultural Adjustment Act, as amended, are hereby reenacted but only for the purpose of allowing refunds in accordance therewith in cases where the delivery

for charitable distribution or use, or the exportation, or the manufacture of large cotton bags, or the decrease in the rate of the processing tax (or its equivalent under section 16 (e) (3)), took place prior to January 6, 1936.

SEC. 602. FLOOR STOCKS AS OF JANUARY 6, 1936.

(a) There shall be paid to any person who, at the first moment of January 6, 1936, held for sale or other disposition (including manufacturing or further processing) any article processed wholly or in chief value from a commodity subject to processing tax, an amount computed as provided in subsection (b), except that no such payment shall be made to the processor or other person who paid or was liable for the tax with respect to the articles on which the claim is based.

(c) As used in this section—

(1) The term "commodity subject to a processing tax" means a commodity upon the processing of which a tax was provided for under the Agricultural Adjustment Act, as amended, as of January 5, 1936.

* * * * * * * * *

SEC. 902. CONDITIONS ON ALLOWANCE OF REFUNDS.

No refund shall be made or allowed, in pursuance of court decisions or otherwise, of any amount paid by or collected from any claimant as tax under the Agricultural Adjustment Act, unless the claimant establishes to the satisfaction of the Commissioner in accordance with regulations prescribed by him, with the approval of the Secretary, or to the satisfaction of the trial court, or the Board of Review in cases provided for under section 906, as the case may be—

(a) That he bore the burden of such amount and has not been relieved thereof nor reimbursed therefor nor shifted such burden, directly or indirectly, * * *.

* * * * * * * * *

SEC. 906. PROCEDURE ON CLAIMS FOR REFUNDS OF PROCESSING TAXES.

* * * * * * * * *

(b) There is hereby established in the Treasury Department a Board of Review (hereinafter referred to as "the Board"). * * * The Board shall have jurisdiction in proceedings under this section to review the allowance or disallowance of the Commissioner of a claim for refund, and to determine the amount of refund due any claimant with respect to such claim. The Commissioner shall make refund of any such amount determined by a decision of the Board which has become final. The proceedings of the Board and its divisions shall be conducted in accordance with such rules and regulations as the Board may prescribe, with the approval of the Secretary.

* * * * * * * * *

SEC. 907. EVIDENCE AND PRESUMPTIONS.

(a) Where the refund claimed is for an amount paid or collected as processing tax, as defined herein, it shall be prima-facie evidence that the burden of such amount was borne by the claimant to the extent (not to exceed the amount of the tax) that the average margin per unit of the commodity processed was lower during the tax period than the average margin was during the period before and after the tax. If the average margin during the tax period was not lower, it shall be prima-facie evidence that none of the burden of such amount was borne by the claimant but that it was shifted to others.

* * * * * * * * *

(c) The "tax period" shall mean the period with respect to which the claimant actually paid the processing tax to a collector of internal revenue and shall end on the date with respect to which the last payment was made. The "period before and after the tax" shall mean the twenty-four months (except that in the case of tobacco it shall be the twelve months) immediately preceding the effective date of the processing tax, and the six months, February to July, 1936, inclusive. * * *

* * * * * * * * *

(e) Either the claimant or the Commissioner may rebut the presumption established by subsection (a) of this section by proof of the actual extent to which the claimant shifted to others the burden of the processing

tax. Such proof may include, but shall not be limited to—

(1) * * * If the claimant asserts that the burden of the tax was borne by him and the burden of any other increased costs was shifted to others, the Commissioner shall determine, from the effective dates of the imposition or termination of the tax and the effective date of other changes in costs as compared with the date of the changes in margin (when margins are computed for weeks, months, or other intervals between July 1, 1931, and August, 1936, in the manner specified in subsection (b)), and from the general experience of the industry, whether the tax or the increase in other costs was shifted to others. * * *

* * * * * * * * *

Internal Revenue Code, Sec. 3443(d):

(d) No overpayment of tax under this chapter shall be credited or refunded (otherwise than under subsection (a)), in pursuance of a court decision or otherwise, unless the person who paid the tax establishes, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, (1) that he has not included the tax in the price of the article with respect to which it was imposed, or collected the amount of tax from the vendee, or (2) that he has repaid the amount of the tax to the ultimate purchaser of the article, or unless he files with the Commissioner written consent of such ultimate purchaser to the allowance of the credit or refund.

Treasury Regulations 81, promulgated under the Agricultural Adjustment Act:

ART. 9. *Exemptions from processing tax.*—

* * * * * * * * *

(b) *Processing by, or for, or for sale to, the United States, a State, or the instrumentality of either.*—Processing for, or for sale to, the United States, a State, a Territory, or a possession, is subject to the tax, whether or not the commodity or the product derived from the commodity is owned by the United States, such State, such Territory, or such possession. Where a State of

the United States is engaged in the business of processing, or in processing and the business of selling the articles resulting from such processing, such processing is subject to tax, and such State is liable, as processor, for the tax. Where a State of the United States is neither engaged in the business of processing, nor engaged in processing and the business of selling articles resulting from the processing, and the processing and disposition of the articles processed are done by the State itself in the exercise of an essential governmental function, such processing is not subject to tax, and such State is not liable for the tax.

SUPREME COURT OF THE UNITED STATES.

No. 45.—October Term, 1941.

The United States, Petitioner, vs. The Kansas Flour Mills Corporation.	On Petition for Writ of Certiorari to the Court of Claims.

[December 8, 1941.]

Mr. Justice Roberts delivered the opinion of the Court.

Between May, 1935, and January 6, 1936, the respondent entered into eight contracts for the sale of flour to the United States. Deliveries were duly made and the contract price was paid. Each of the eight contracts provided:

"Prices set forth herein include any Federal tax heretofore imposed by the Congress which is applicable to the material purchased under this contract. If any sales tax, processing tax, adjustment charge or other taxes or charges are imposed or changed by the Congress after the date set for the opening of the bid upon which this contract is based and made applicable directly upon the production, manufacture, or sale of the supplies covered by this contract, and are paid to the Government by the contractor on the articles or supplies herein contracted for, then the prices named in this contract will be increased or decreased accordingly, and any amount due the contractor as a result of such change will be charged to the Government and entered on vouchers (or invoices) as separate items."

Under the terms of the Agricultural Adjustment Act,[1] processing taxes were due in respect of the flour sold aggregating $28,419.20.

In 1936 the respondent entered into four contracts for the sale of flour and bran to the United States for a total price of $23,288.11. The commodities were delivered and vouchers for the purchase price tendered to the General Accounting Office. Payment was withheld by the Comptroller General who notified the respondent that the Government had overpaid it in the sum of $28,419.20.

The respondent had obtained an injunction against the collection of any processing taxes from it and, as a result of the decision

[1] U. S. C. Supp. V, Tit. 7, § 609.

in *United States* v. *Butler*, 297 U. S. 1, paid no processing taxes on the wheat used in the manufacture of flour covered by the 1935 contracts.

The respondent sued in the Court of Claims to recover the purchase price under the four 1936 contracts and contested the offsets claimed by the Government arising out of the eight 1935 contracts. Judgment was rendered in favor of the respondent for $23,288.11. We granted certiorari because of the importance of the question[2] and of the number of pending cases involving the same question. We are of opinion that the respondent was not entitled to recover.

The contracts are to be construed in the light of the relations between the parties at the time they were executed. The Agricultural Adjustment Act did not exempt a vendor to the United States from the processing tax; and a Treasury Regulation required that he pay the tax.[3] The quoted clause shows that this tax was specifically in the minds of the parties, for it was stipulated that it was included in the price bid. The Government stood in a dual relation to the respondent. It became, at the same time, a purchaser at the named price and also a claimant of the processing tax upon the material purchased. The stipulation was evidently made in view of the facts that the purchasing officer could not buy the goods tax-free and that the Government desired that the price to it should be ex-tax. To accomplish this the sale price was *pro tanto* offset by the amount of the tax. Plainly, if the United States had not been thought entitled to collect the tax, the bid price would not have been acceptable. Plainly, also, if the respondent had not been thought liable for the tax, the bid price would have been less.[4] As disclosed by the contracts, the understanding was that the price would have been less by the amount of the tax. The respondent disputes this, contending that we cannot say how much of the tax it was willing to absorb in order to obtain the contracts; that it may have been making the sales at an actual loss. But this is not the theory of the contracts. They provide that if, in future, any existing tax described therein is changed by Congress the price named in each contract "will be

[2] United States v. Hagan & Cushing Co., 115 F. 2d 849; Ismert-Hincke Milling Co. v. United States, 90 C. Cls. 27; United States v. American Packing & Provision Co., 122 F. 2d 445.

[3] Regulations 81, Art. 9, under the Agricultural Adjustment Act.

[4] Compare United States v. Glenn L. Martin Co., 308 U. S. 62.

increased or decreased accordingly." This does not mean, as contended by respondent, that the amount of increase or decrease is an unknown quantity to be made definite and certain by proof. It means that the amount of any increase in tax shall be added and the amount of any decrease subtracted from the contract price. This view is strengthened by the provision for separate billing of the increase, if any.

The respondent, however, argues that, under any construction, the Government is not entitled to maintain its set-off, first, because the contracts contain no undertaking by respondent that it will pay the tax and, secondly, that, even if they do, the stipulation for reduction of price applies only to changes by Congress and excludes relief from the tax by an adjudication that the exaction is unconstitutional.

In support of the first proposition, the respondent relies on numerous decisions holding tax clauses in private contracts not to require adjustment of the contract price as a result of the decision in the *Butler* case, *supra*.[5] These go on the absence of an express provision respecting the constitutional validity and upon the omission of the parties to bill the tax separately from the purchase price. We think they are inapplicable in the present case since the tax clause here had a purpose different from those in private contracts. As we have said, the purpose here was to deprive either party of the advantage or disadvantage resulting from the incidence of the tax and, therefore, it was sought to eliminate the effect of the exaction on the contract price.

In the case of private contracts, the vendees purchase for resale and the tax burden assumed is passed on to their customers. The fact that the processor—the vendor—is protected from the payment of the tax by injunction does not reduce the price to the vendee or to purchasers from him. The courts will not permit the unjust enrichment involved in recovery by the vendee of the amount of tax which he has passed on to his creditors.[6] In the contracts in

[5] Moundridge Milling Co. v. Cream of Wheat Corp., 105 F. 2d 366; Consolidated Flour Mills v. Ph. Orth Co., 114 F. 2d 808; United States v. American Packing & Provision Co., 122 F. 2d 445; City Baking Co. v. Cascade Milling & Elevator Co., 24 F. Supp. 950; G. S. Johnson Co. v. N. Sauer Milling Co., 148 Kan. 861 (1938); Sparks Milling Co. v. Powell, 283 Ky. 669 (1940); Crete Mills v. Smith Baking Co., 136 Neb. 448 (1939).

[6] See the cases cited Note 5. The respondent urges that the unjust enrichment tax imposed by Title III of the Revenue Act of 1936 (49 Stat. 1734) destroys the equity of the Government's case, but if respondent is required

question, the Government did not buy for resale. Unless it received the tax it suffered a definite disadvantage.[7] Its purpose, as shown by the contracts, was to balance the tax element in the price paid with the tax collected.[8] The Government, which could not pass on the tax on resale, was thus protected, not against a fall in the market price but against a loss in its tax revenues. In cases of private sales, the processor's injunction against collection of the tax, as held by the cases cited, worked no harm to his vendee. A similar injunction, in the case of Government contracts, would leave the price to the Government at the higher level reflecting the tax and deprive the Government of the reciprocal benefit flowing from collection of the tax.

In its second position the respondent attempts to meet what has been said as to the inequity of its retaining the full price, when it escapes paying the tax, with the argument that the result is inevitable under the contracts. It refers to the fact that it had already obtained an injunction against the collection of the processing tax when some of the 1935 contracts were made and asserts that if the Government desired to provide against a decision that the taxing act was unconstitutional this could readily have been done by the addition of a single phrase.

As we have said, there is respectable authority for the position that tax clauses in private contracts do not reach a judicial decision of invalidity of the statute. We think, however, these decisions have no application in the present instance. Here legislation recognizing the decision in *United States* v. *Butler*, *supra*, and imposing taxes on the enrichment of those who passed on the amount of the tax without having to pay it, may properly be said to have been a change of the tax by Congress within the terms of the contracts.

The decision in the *Butler* case was rendered January 6, 1936. It is true that after that decision a taxpayer's right to an injunction against the collection of the tax was clear.[9] But, by the Revenue

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to reduce its price by the amount of its unpaid processing tax it will not be subject to the unjust enrichment tax on these transactions. See §§ 501(b)(2) and 501(j)(4).

[7] In United States v. American Packing & Provision Co., 122 F. 2d 445, the Government was held entitled to maintain a set-off asserted under conditions like those here involved on the ground that the vendor had received money from the Government which in equity and good conscience it should repay.

[8] Compare United States v. Cowden Mfg. Co., 312 U. S. 34, 36-37.

[9] Rickert Rice Mills, Inc. v. Fontenot, 297 U. S. 110.

Act of 1936,[10] which became a law June 22, 1936, Congress not only recognized the effect of that decision as doing away with the tax in question but legislated with respect to the consequent rights and remedies of those who had paid the tax and the liability of those who had passed on its burden and escaped payment.

By Title III a tax is laid on the unjust enrichment consequent upon the passing on to customers the burden of unpaid processing taxes. In § 501(b)(i)(2) and (j)(2) Congress defines the date of termination of the tax as "*in the case of a Federal excise tax held invalid by a decision of the Supreme Court, the date of such decision.*" In Title IV there is a provision relative to floor stock taxes which recognizes the invalidity of the Agricultural Adjustment Act by reenacting the refund provisions of that Act in respect of transactions prior to January 6, 1936, the date of the *Butler* decision. (§ 601(a).) The title defines a taxable commodity as one on which a processing tax was provided for as of January 5, 1936, the day before the *Butler* decision. (§ 602(c)(1).)

Title VII makes provision for the refund of processing taxes collected under the Agricultural Adjustment Act and is a recognition by Congress that the taxes were invalid.

Thus a change in respondent's tax liability has been recognized and confirmed by Congress. Even though this legislative action was a confirmation of or acquiescence in the *Butler* decision, and although its effect may have been merely cumulative, it amounted to a change made by Congress in respondent's liability for the tax, within the meaning of the contracts.

The judgment is reversed.

A true copy.

Test:

Clerk, Supreme Court, U. S.

[10] 49 Stat. 1648.